

**CAN A DEVELOPING DEMOCRACY MANAGE ITS
MACROECONOMY? THE CASE OF THAILAND**

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Introduction

The East Asian miracle has generated a vast literature which examined the sources of growth, both in the narrow growth-accounting sense, and in the broader sense that brings issues of governance and policy-making processes into consideration. Parts of East Asia have had authoritarian regimes, and there is a certain amount of controversy as to whether this feature has in fact contributed to their rapid growth. On the other hand, it was agreed by all participants that East Asia (in contrast to, say, Latin America) managed its macro-economy better. It was posited, certainly by the World Bank study on the East Asian miracle, that this better macroeconomic performance was at least partly responsible for the higher growth in East Asia (World Bank 1993:12-13,105-123).

Thailand has featured in some of these analyses, even though it is in some respects exceptional to the rest of East Asia. For one thing, it has had a spottier political history. It has not been "blessed" by stable governments lasting into decades. Authoritarian regimes alternated with democratic regimes, with the authoritarian interludes becoming briefer and rarer over the last few decades. Nonetheless, Thailand has had good growth performance with macroeconomic stability, at least until 1996. Because it shared this stability with its East Asian neighbors, it could be used to make the point that macroeconomic stability was sufficient to guarantee growth.

Those who have examined Thai economic policy in any detail have shared a common belief that there is a bifurcation in its performance. They claim that the government managed the macro-economy superlatively under both authoritarian and democratic regimes, even though its sectoral policies left a great deal to be desired (Christensen, Ammar and Pakorn 1992; Doner and Ramsay 1997). The good macroeconomic performance was partly attributed to the presence of a highly competent technocracy insulated from the patronage politics that thrived in sectoral policies.

However, the catastrophe that hit Thailand this year requires a revision of the all too sanguine view concerning its capability to manage the macroeconomy, and the associated view that that capability resided in a politically insulated technocracy. It is that revision which I shall essay in this lecture.

The argument in this lecture will be developed in three stages. In the first stage, it will be shown that although the root cause of the Thai crisis of 1997 lies in excessive borrowing by the private sector, its effect has been multiplied by misguided policies, particularly those emanating from the Bank of Thailand. The enumeration of policy mistakes provides only an incomplete picture however, since the Bank of Thailand was once renowned for its capability and integrity. An explanation has to be found for its strikingly poor performance in the 1990s. Therefore the second stage develops a set of reasons why the Bank's performance, and that of the technocracy in general, declined. Finally, since the failure of the technocracy could in principle be ultimately corrected by the political leadership, it has to be explained why the Thai political system failed to deliver that leadership.

Economic Collapse

The first and most important point to be made about the current Thai crisis is that it is based entirely on excessive private rather than public debt. The level of public debt in Thailand has in fact been getting steadily lower, whittled down by years of fiscal surpluses. At the end of 1996, domestic and foreign public debt, including the government-guaranteed portion of the state enterprise debt, stood at only \$27.9 billion or about 15 per cent of GDP, which surely would place Thailand as one of the least publicly indebted countries in the world.

By contrast, the local corporate sector's total indebtedness has been very high. Thai capitalism is largely based on family businesses; even companies listed in the stock exchange remain entirely so, except for subsidiaries of the multinationals. As the economy grew, these businesses grew in tandem, in many cases even faster. By and large, the families displayed little willingness to relinquish control over their firms. Consequently, the firms borrowed heavily to meet their need for capital. And their debt dependence grew steadily. Thus, the average debt/equity ratio of listed nonfinancial companies rose from 1.58 to 1.98 between 1994 and 1996, as their interest cover (earnings before tax and interest payments/liability) fell from 14.2 to 10.7 per cent (figures provided by Phatra Research Institute), making them highly vulnerable.

This corporate debt problem has an important foreign component. The debt owed by the non-bank private sector to foreigners stood at US\$63.0 billion at the end of 1996, of which as much as \$29.2 billion has a duration of less than one year. (To help put these figures in proportion, the gross domestic product in 1996 at the then prevailing exchange rate was \$194 billion.) Foreign corporate debt grew particularly rapidly during 1994 and 1995, associated with the opening of the Bangkok International Banking Facility (BIBF), which I shall describe in detail below.

True, while corporate debt was growing, the equity market also made great strides. But as the movement in the debt/equity ratio given above made clear, the equity was not used to lower the debt dependence. Rather, it was used to leverage more debt.

A significant portion of the proceeds from this increasing debt was used to buy land and invest in real estate. Real estate loans play a key role in the Thai credit market. They were provided by banks and the finance companies (the latter are deposit-taking institutions with some restrictions in the type of deposits they can accept). Financial institutions provide loans more readily when land or real estate is put up as collateral. Normally of course, the amount of loans provided is less than the value of the collateral. But when land prices were rising rapidly, as during the boom years of 1988-1995, the investment in land and real estate paid off additionally in terms of the ability to float more debt. Part of the increased debt was used to purchase even more land which drove its prices further up, and so on. Clearly what was emerging was a build-up of a debt pyramid, which could last as long as the growth rate of the economy and the consequent growth in asset prices were kept up. A slowdown in the growth of land prices would have brought the system crashing down.

The economy was already slowing down from the heady two-digit levels in 1988-1990 with the onset of the Gulf war in 1991, but it was still quite high at more than 8 per cent per annum, which was considered then to be the normal rate of growth for the Thai economy. Demand for real estate continued to be brisk, but building was

proceeding at such a rapid pace that it was a matter of time before there would be an excess supply.

Vulnerably for Thailand, a great deal of this borrowing, used primarily to invest in long-term assets, was from the financial institutions, whose main sources of funds were relatively short-term deposits. True, a domestic bond market was being developed in the mid-1990s but was still quite small when the crisis struck.

With such an asset bubble, it is little wonder that the total investment in the Thai economy rose as high as 42 per cent. But with increasing investment rate, the growth rate stayed stubbornly at 8 per cent per annum, raising the incremental capital/output ratio to 5 – a ratio more characteristic of socialist economies than what was taken to be a vibrant capitalist one.

But to say that the crisis has its origins in private borrowing is not to absolve the government from blame for the resulting problems. The first misstep made by the authorities was the decision to open up the capital account.

In March 1993, the Bank of Thailand introduced the Bangkok International Banking Facility (BIBF), apparently with the intention of making Bangkok a financial center that would eventually vie with Singapore for business with the transitional economies of Southeast Asia. However, it soon transpired that most of the business generated by the BIBF was to facilitate lending by foreigners to Thai firms, with the banks acting as intermediary. All such transactions, including the on-lending by banks to firms, were to be done in foreign currency.

Within less than four years, the amount lent through BIBF rose quickly from nothing to reach \$31.2 billion by the end of 1996, or almost a half of total private foreign debt. It is to be noted that much of the lending, which was at lower interest rates than that from domestic sources (see below), went into the capital-intensive sectors such as chemicals, petroleum and construction sectors (Bank of Thailand 1996b:7).

Opening the capital account is not by itself necessarily bad. The second misstep was to retain a fixed exchange rate regime alongside the open capital account.

The BIBF was popular with borrowers because the interest rate on the dollar loans was 4-6 per cent lower than domestic rates. This differential refused to go away with the influx of foreign money even when the cost of forward cover is included, for reasons that are still not clear to me.¹ Regardless of the cause of the differential, from the borrower's point of view the cheap loans were very attractive, and they continued

¹ The econometric work that I am aware used data mostly from the 1980s, which preceded the establishment of BIBF and indicates perfect or near perfect capital mobility already during that decade, in the sense that local interest rate *movements* reflect international interest rate movements almost point by point. (Robinson et al. 1991:39-42; Rungsun Hataiseree and Phipps 1996; Warr and Bhanupong 1996:171-178). Nevertheless, the difference in the *levels* of interest rates has persisted and been quite high, both then and after 1993. It could be argued that this difference reflected expectations of a devaluation. Warr and Bhanupong used data on the forward premium during the 1980s to test this argument and found that the data do not support either the nominal interest-rate or the real-interest rate parity hypotheses.

to borrow merrily, presumably confident in the strength of the baht, a confidence bolstered by the high level of reserves which stood at about nine months of imports. Moreover, most of the loans contracted with the BIBF were of short duration, and loans by non-financial companies were usually uncovered. Financial institutions are required by the central bank to hedge most of their foreign-currency borrowings.

The heavy inflow of foreign capital occasioned by the establishment of the BIBF had three consequences. First, the BIBF gave a second wind to the property boom. As early as 1994, it has become obvious to observers of the real estate scene that the dreaded excess supply situation had arrived. Sales were beginning to falter. Without the BIBF, the country would have been facing a credit crunch and the collapse of real estate companies (and perhaps some finance companies) at least a few years earlier. It is arguable that in that case the collapse would have been less spectacular.

Secondly, the high volume of foreign borrowing led to a rise in the real exchange rate. Baht and dollar inflation rates were running roughly in parallel until 1994, when the former began to inch up to 5 and approached 6 per cent (year-on-year comparison), while the latter was heading downwards to 2 per cent.

The third impact was on the current account deficits which soared to 8 per cent of GNP, but with a rapidly rising exports (ranging from 15 to 20 per cent per annum), it could be argued that such increases in indebtedness could be accommodated. However, a sign of trouble showed up unmistakably in the second half of 1996, when, quite suddenly, the export growth rate sank to zero per cent. It is still not clear what caused this abrupt decline, but the increase in real exchange rate was at least partly to blame.

Despite these signs, the Bank of Thailand committed its third misstep by refusing to take action on the exchange rate. Instead, it blustered its way out by arguing that:

- the large current account deficit, at least upto 1995, was cyclical, and was connected with a temporary investment upturn occasioned by increasing capital utilization, industrial upgrading, infrastructural investment and a surge in the Board of Investment promotion (Bank of Thailand 1996a);
- while the BIBF loans did lead to an observed shortening of the average maturity of Thai foreign debt, this was partly a statistical illusion caused by the diversion of borrowing source to the participant bank, which if foreign, used revolving funds (appearing as short-term inflow in the Thai balance of payments) to finance their long-term loans to local companies (Bank of Thailand 1996b:8-9);
- in any case, the short-term debt posed little risk to the Thai economy, as it was covered by adequate foreign exchange reserves, and also because the strong fundamentals would rule out the possibility of a flow reversal (Bank of Thailand 1996b:16-17);
- the export stagnation recorded in the second half of 1996 was temporary, owing to a decline in world trade growth, supply shortages in the fishery

sector due to diseases and a maritime dispute with a neighboring country, and to the lessening competitiveness of the more labor-intensive sectors, and was expected to recover to a growth of 7.7 per cent in 1997, “on account of the resurgence of demand from trading partner countries, as well as the impact from export promotion measures” (Bank of Thailand 1996c:6, 11-12)

Much of these we now know of course to be wishful thinking. But in 1996 and in the first half of 1997, as a consequence of these beliefs, the Bank of Thailand persisted in defending the old exchange rate against at least three major attacks by foreign speculators, in November 1996 and in February and May 1997. The reserve depletion from these attacks was hidden from the public by the forward sale of its dollars to support the baht. Nevertheless, even the reported foreign exchange reserve came down from \$40 billion at the beginning of 1997 to \$33.8 billion at the end of June, on the eve of the flotation of the baht. This small fall in the reserves masked the true situation, for it was known at the time that the *net* foreign exchange position was much worse. To defend the currency, the Bank of Thailand entered into large forward commitments. It was later revealed that the foreign exchange position, net of these forward commitments, went from \$33 billion in the beginning of the year to a mere \$2.5 billion at the end of June 1997. Consequently, when the Bank of Thailand floated the baht on July 2, it was done with essentially zero foreign exchange reserve.

In addition to the decline in the foreign exchange reserve, there were also increasing claims on the central bank's other assets, primarily from the imploding financial system. Here we come to the fourth, and probably the most damaging misstep, or perhaps a series of missteps from the Bank of Thailand.

A precursor of the 1997 implosion in the financial system was the troubles of the Bangkok Bank of Commerce (BBC), a small bank. It had been ailing for some time when, in 1994, the central bank began to take a much closer look, and eventually sent its representative to the board of the bank, but not until after it botched its first attempt by being simply outvoted at a shareholder's meeting. It soon became clear that there were some strange practices going on within the BBC, and the central bank even submitted a brief to the Attorney-General's office for criminal action against some of BBC's former senior executives. But that brief was submitted too late for possible action before the statute of limitations ran out. The botched attempt at a takeover of management and the failure of the criminal action are merely two of the many examples of the way the central bank mismanaged the BBC affair. In 1996, parliamentary debates revealed to the public the extent of politically motivated loans made by the previous officers of BBC. A run began to develop and continued causing the Bank of Thailand to pour in almost US\$7 billion (at the then exchange rate) from its Financial Institution Development Fund (FIDF) to support it.

As the real estate market collapsed in 1996, rumors concerning the loan problems of the finance companies began to spread, fanned in March 1997 by the central bank's publicly announced action requiring ten of them to raise their capital within 60 days. They were however allowed to remain open. Consequently, there began to be runs, first on these finance companies, but later on, on others and on the smaller banks as well. The illiquidity caused by these runs was covered by further loans

from the Financial Institution Development Fund (FIDF), which is attached to the Bank of Thailand. In June, sixteen finance companies including seven of the original ten, were suspended from operations and were told either to find additional capital or to merge with other firms.

These finance companies' suspension raised the fear that the Bank of Thailand would end up shouldering a good part of the losses incurred by these illiquid and possibly insolvent firms. This belief stems from action taken by the Bank in earlier cases of failures. Each time the finance companies were suspended during 1997, there would be pronouncements from senior officials that all deposits will be guaranteed. There was also talk of the guarantee being extended to the creditors of the finance companies as well.

Most importantly, during the runs on the finance companies, the Bank of Thailand was forced to provide credit to the FIDF. This led to a rapid expansion of the monetary base, which increased 10 per cent in one month (June 1997) alone.

Clearly, the Bank of Thailand could not continue to support the baht internationally and illiquid finance companies domestically. This was well recognized by the markets. Consequently, the attacks on the baht continued to increase in intensity. After May 1997, ordinary Thais were joining foreigners and the banks in the attack. On July 2, 1997, the Bank of Thailand finally bowed to the inevitable, and allowed the baht to float in a system which it bravely called a "managed float". Since most market operators knew or speculated that the Bank had run out of reserves, the exchange rate was freely floating (actually "sinking" would be a more accurate description) more than it was managed. The value of a baht has steadily deteriorated until it now (May 21, 1998) stands at some 33 per cent below the level on July 1, or the price of a dollar has increased 50 per cent.

On the domestic front, the financial companies continued to need infusions of money from the central bank's FIDF. Simultaneously with the announcement that Thailand had requested the support of the International Monetary Fund in August 1997, another batch of 42 finance companies were told to suspend their operations, bringing the total number of finance companies suspended to 58, out of the original 91. In December, 56 of these were permanently closed.

Because of the exchange rate mismanagement and the meltdown in the financial sector, Thailand is now poised at the edge of what will probably turn out to be the most severe slump it has experienced in the last four decades.

The Decline of the Technocracy

Thai macro-economic policies have been mostly made by technocrats. The policy failures of the last few years can be laid fairly and squarely on them, or to be more specific, on the officials of the Bank of Thailand. Given that the Bank, and the technocrats more generally, were once highly respected, the question naturally arises as to why they became so spectacularly incompetent all of a sudden. To answer the question, a historical detour is necessary.

Strictly speaking, the technocracy managing the country's macroeconomy consisted of officials from the Ministry of Finance, the Bank of Thailand, the Budget Bureau and the planning agency. This group emerged as a result of a major overhaul of the country's economic management system during the regime of Field Marshal Sarit Thanarat, a dictator who ruled Thailand between 1958 and 1963. Under him and his immediate successor, that is until 1973, this technocracy enjoyed considerable autonomy and managed to keep at bay the demands of the military who at that time occupied key political posts.

The relationship between the technocracy and its military rulers was far from smooth. The latter's need to expand government budget in general and the military budget in particular was a constant cause of conflict, as were some of their corrupt activities which entered the radar screen of the technocrats (for example, contracts to print bank-notes). But by and large, a *modus vivendi* was achieved, because both shared the vision that the economy needed to grow which for the technocrat was the desired aim, and for the military, was the means by which they could obtain greater spoils.

The emergence of a more open politics since 1973 did not necessarily witness a linear trend toward democracy. The role of the army, in particular, waxed and waned, and with it the power of the technocrats. By and large, during the post-1973 period, the rise in the power of the army tended to see the power of the technocrats in macro-economic management rise. Similarly, whenever the army's power waned, the power of the technocrats would go into eclipse. Because of the need for patronage on the part of the elected politicians, technocrats began to have an adversarial relationship against them, and naturally sought the army as allies to push their case and to protect them. But one must not conclude that the technocracy necessarily became powerless every time the military disappeared from the scene.

For more recent years, it is necessary to refine the notion of technocracy further and break it down to at least two sub-groups. One sub-group, in charge of monetary policy, would be the Bank of Thailand, with its own tradition and ethos, which are quite distinct from the others. These others consist of civil servants in the Ministry of Finance, the Budget Bureau and the planning agency, who are primarily in charge of the country's fiscal policy. I shall discuss this latter sub-group first.

The evolution of this latter group is part of the general evolution of the Thai civil service. Over the years, the quality and competency of the Thai civil service has been declining, precipitously during the last decade. During its heyday, the technocrats used to enjoy considerable autonomy in the formulation of the country's fiscal policy, but with the erosion in quality, this autonomy has steadily eroded. But, until this year, the decline has not seriously affected the outcome, for coincidentally, the last decade has seen an unprecedented boom in the economy, which generated rapid increases in government revenue. Indeed so rapid were these increases that even our politicians were unable to generate enough expenditure projects to absorb the increases. Consequently, the country had been enjoying a long series of fiscal surpluses, which have now come to an end, and has been putting a severe strain on our fiscal policy machinery.

The history of the Bank of Thailand is quite different, however. The structure, organization and ethos of the Bank of Thailand was established during the 1950s and the 1960s, by the then governor of the Bank, Dr. Puey Ungphakorn, a revered figure among the country's technocrats and academics. The institution that he led was imbued with a spirit of fierce integrity. In a country in which corruption is rife, the Bank of Thailand was considered to be the only institution where it was unthinkable that any corrupt practices could be found. This reputation of incorruptability gave it considerable moral authority and prestige and allowed it to enjoy *de facto* autonomy, overriding its *de jure* subservience to the Minister of Finance.

Another of Dr. Puey's legacies was the expenditure on the Bank's human resource development. It spent more on this than probably any other organization, public or private. Thus, in 1995, approximately 160 persons, chosen from among the top students in Thai schools and universities, were receiving Bank of Thailand scholarships to study in some of the world's most outstanding universities. Clearly, insufficient training cannot be blamed for the Bank's disastrous performance in the last few years. That such individual capabilities could lead to collective incompetence can only be explained by a faulty management structure.

The management structure designed for the 1960s is no longer relevant for the present-day distribution of human resources within the Bank itself. During the 1960s, there was a clear gap between senior management and the rest of the staff in terms of age, experience and authority, a gap that was emphasized rather than offset by the charisma that is peculiarly Dr. Puey's. A management structure was therefore designed with the internal power of the Bank very much concentrated in the hands of the Governor who, it was thought, would shield the Bank from the depredations of the military government of the time. This concentration of authority in the hands of the Governor worked as long as the gap in seniority and authority between the top and lower levels of management remained.

However, with the scholarship program of the 1960s beginning to bear fruit, the graduates returned to fill up the middle management and began to rise through the ranks. A critical turning point was the appointment to the governorship of Vijit Supinit who had been in the first batch of scholars sent abroad. By this time the men and women who were trained under the scholarship have filled up the senior and middle management levels of the Bank. In terms of intrinsic ability, the Governor is now only first among equals; in terms of legally vested powers, however, he is very much at the top. As a consequence, the prize of governorship and the fight for it among the top management became a very important backdrop that undermined effective teamwork. Additionally, as the Bank staff tended to pursue a lifetime career within it, competition among the staff led to severe factionalism within the Bank. As a result of all this, the pool of available talent was not put to effective use, and worse, the dedication to the public interest that suffused the Bank's ethos in the period before 1990 has all but disappeared.

Externally, the Governor is accountable only to the Minister of Finance. Increasingly, his position is being held at the pleasure of the Minister. The Governor does not have a fixed-term appointment, but can be dismissed by the Minister of Finance – a previously rare event, but which was beginning to occur with increasing

frequency (of the five governors holding the position in the 1980s, two were dismissed). This trend has made probable what I would call “implicit interventions” by the Minister of Finance, that is, instead of submitting to explicit orders from the Minister, the Governor would anticipate the Minister’s desires and followed the current political line.

However, by and large, the Ministers of Finance, regardless of whether they were former technocrats or elected politicians, were content to let monetary policy and the supervision of the financial institutions be largely in the hands of the Bank. Points of conflict have centered around exchange-rate policies more than any other aspects of the Bank’s activities (although interest-rate policies are beginning to be contested as well) (Rangsun Thanapornpun 1996:84-85). As both the Bank and the Ministry of Finance naturally wish to minimise conflict, the authorities have gravitated toward a fixed exchange-rate regime, and ran the monetary policy to achieve the simple target of maintaining the pegged rate. More importantly, when the time came to alter the pegged rate as at the beginning of 1997, it appears that the Bank of Thailand was reluctant to do so partly for fear of *political* repercussions, an example of implicit intervention.

Combining my observations that the civil service section of the technocracy has declined and that the Bank of Thailand has severe internal tensions, I conclude that it is a dispirited and demoralized technocracy that confronted the economic crisis. Indeed it is doubtful even whether an autonomous technocracy exists any more. True, the Bank of Thailand is still very much in charge of monetary policy (including exchange-rate policy) and of the supervision of financial institutions, but it has been so badly wounded by the BBC affair that it no longer has much authority with the public to obtain adequate support for its actions. The fiscal-policy side of the technocracy has clearly disintegrated. The degree of cooperation between the four key agencies is now minimal.

With a non-functioning technocracy, political leadership becomes an essential backstop. It is here that our parliamentary system failed us badly.

Political Negligence

Since 1992, the form of government in Thailand has been parliamentary in as full a sense of that term as it has ever been, in that there has been little extraparliamentary pressure put on the governance of the country. However, even though it has now fully flowered, the Thai parliament had grown in the shadow of governments dominated by the armed forces. It has thereby acquired certain habits which ill equipped it to deal with the kind of problems Thailand now faces.

In the past, when the military were active in government, the central national policy issues were their domain or that of their allies, the technocrats. Fenced off from this domain, the parliamentarians played their representative role to the hilt. To them, and more importantly, to their constituents, the public treasury is a milchcow, and the MPs' central chore is to milk that cow, and bring the milk back home to their constituents. This arrangement was subject to the caveat that total public expenditure was under the control of the technocrats. Consequently, much of the struggle centered around the allocation, with very little said of the size of the budget, and still less of

taxes. Indeed, most of the moves towards tax cuts during the boom were initiated by bureaucrats from the Ministry of Finance.

Obviously, the use of taxpayers' money was not the only means by which a politician could bring benefits back to their home constituencies. In the *modus vivendi* that emerged in the 1980s between the military and their technocrats, on the one hand, and local politicians, on the other, parliamentarians acquired the sectoral ministries: agriculture, industry, commerce, and communications, for example (Christensen, Ammar and Pakorn 1993). These ministries generated considerable amounts of corruption money. As the economy grew, this corruption money grew in tandem, certainly in absolute terms, although whether it grew relative the size of the economy is a moot point. But in any case, a politician, if he or she is to survive, has to channel a portion of this corruption money back to the constituents.

The key consequence of this development is in the expectations among the constituents, particularly in the rural areas. It is now widely expected that politicians will bring projects into their constituencies. It is widely expected that such projects will generate side benefits to the rural elite, who are quite active in the construction business. It is therefore widely expected that when the politicians and the rural elites are up for elections, money will flow and votes will be bought. Money politics has become the norm, and politicians are judged by their effectiveness in bringing home the money from Bangkok. Constituents are aware of what their representatives are up to there, but do not seem to care. It can even be claimed that they are happier, the more corrupt their representatives are, because that means more money from Bangkok.

Consequently, in the competitive arena of Thai democratic politics, a politician's ability to formulate clear *national* economic policies, even those biased toward the rural areas in general, does not weigh very highly in the electors' consideration. Political parties have very little interest in developing this sort of talent or of establishing connections with pressure groups to help them formulate a coherent set of policies. True, political parties have lines of communications with business, and many of the politicians are themselves businessmen, but these connections serve mostly to raise corruption money, through the grants of projects and concessions to individual firms. More importantly, the business influence sometimes leads to distortions of national policies – distortions that are not challenged in parliament even if they sometimes blatantly favored particular businesses.

That elected politicians are generally not interested in national policy issues is demonstrated in their attitude to the Ministry of Finance, which is the central organ for the formulation of macroeconomic policy. Thai politicians are as keen on gaining office as politicians anywhere else, and one would expect that this key ministry would be fiercely contested. However, they have generally shied away from it. They have been happy to see this particular post filled by former technocrats or bankers.

Of course, there are exceptions to this generally bleak picture of politicians. Not all politicians are corrupt, nor do all segments among the electorate expect patronage money. But these exceptions are precisely that: exceptions. They have not been able to undermine the majority predilection for corruption and patronage, and for the accompanying parochial politics.

It is therefore not altogether surprising that when the economic crisis hit Thailand in 1996 and increased in intensity in 1997, the public authorities should find themselves in such disarray. In the end, a financially, institutionally and politically bankrupt Thailand had to go cap in hand to the International Monetary Fund.

The Way Out

Unusually, at the time of IMF's entry, the move elicited an overwhelmingly favorable response from Thai opinion leaders. Resisting that entry until the very last moment was the Bank of Thailand, in the past always a receptive interlocutor of the IMF and also of the World Bank. The IMF was regarded so favorably because many in Thailand had come reluctantly to the view that our institutional and political system was incapable of assembling a coalition to support the package of measures needed to head off a catastrophic fall in the economy.

Not that the package which the Thai government signed on to was in any way difficult to fathom intellectually. It was as conventional a package as any from the IMF, and any economist worth his salt, with the kind of information that the IMF had, could come up with a similar one. The gap which the IMF filled in was a gap in authority. The Thai government had to sign away its right to manage its own economy, because by August 1997, that was the only thing it was capable of doing.

I have argued above that the crisis appeared first as an economic and financial crisis. It led to an exposure of the technocratic incompetence and failure, which could not be overcome by our political leaders, because the problem was beyond their comprehension. Does this mean that Thailand is from now on condemned to decades of macroeconomic mismanagement, relieved from time to time by an IMF bailout?

All hope may not be lost. The only bright occurrence in our *annus horibilis* was the passage of a new constitution. This new constitution embodies provisions that are a radical departure from previous ones. Such is the extent of the change in the rules of the game that it is difficult to forecast the outcome of the new elections. It is to be hoped that a new government coming to power as a result of these new rules would be different in kind from the ones to which we have been condemned in the past few years.

The reason for hope rests with the expected change – in the long run – in the complexion of the new parliament. For alongside 400 members elected from individual constituencies, there will be a further 100 members belonging to party lists to be elected nationally. More importantly, it is likely that each party will have on this list individuals whom it expects to nominate to be ministers.² It is expected that these members will take a less localistic stand on issues and will initiate debates on more national issues.

² In another provision, MPs who become ministers are expected to resign their membership in parliament. A vacancy among members elected from the party list will be filled by drawing on the next person on the list of the departing member's party, whereas a by-election has to be held to fill a vacancy among those elected from the constituencies. Clearly, it is safer for a party to retain its numerical strength in parliament by choosing its ministers from among their party-list members than to risk a by-election.

It is hard, however, to imagine a total turnover in the membership of parliament, particularly that section of 400 that will be elected from local constituencies. The current politicians have deep social roots in the Thai countryside, and a mere rewriting of rules cannot be expected suddenly to overcome that fact. Nonetheless, the crisis into which the country has fallen may change the behavior of the politicians. After all, that these much maligned individuals allowed the passage of a constitution that most of them regarded as being directly adverse to their interests, but which they had persuaded themselves is in the public interest, speak much for their sense of patriotism.

Another move that these parliamentarians made soon after the passage of the new constitution was to bring into office of Prime Minister Chuan Leekpai, head of the Democratic Party. He and his party are known for somewhat more concern for the public interest than is prevalent among Thai politicians. Above all, his party seems to have a monopoly of talent in macro-economic management. Consequently, the new prime minister has to cast outside for a Finance Minister, but has within his own Party, not one, but many individuals capable of performing the task. In contrast the previous government witnessed an uneasy relationship that prevailed between the Finance Minister and the rest of the political leadership, which had considerable adverse consequences on the way the economy was managed.

The government has given a sense of relief to the country. Outwardly, it still adheres faithfully to prescriptions from the IMF, but one has the sense that it does so out of conviction, rather than because it does not know any better. Also, as far as prospects in the short term are concerned, there is really very little choice for any Thai government.

For the longer term, the task that still needs to be performed are:

- A reform of the Bank of Thailand, together with the assembly of a machinery for monetary policy for, with a flexible exchange rate, the task of formulating it is no longer trivial as it was in the past;
- A reform of the system of financial supervision and regulation, together with (possibly) an introduction of an explicit deposit insurance scheme;
- A reform of the machinery for fiscal policy formulation and the establishment of a mechanism to link it with monetary policy. This has become even more important, as Thailand needs to move toward a fiscalization of the enormous cost of the support of the financial institutions, estimated at not less than ten per cent of the GNP.

In crafting these reforms, a clear relationship between the policy and the technical level has to be mapped out. I have purposely used the word “technical” rather than the more overpowering “technocratic”, because the country’s political evolution has to be recognized.

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